



CITY OF FALLS CHURCH

December 1, 2011

Anthony H. Griffin
Fairfax County Executive
12000 Government Center Parkway, Suite 552
Fairfax, Virginia 22035

Re: Proposed Amendment to County Code Section 68-6, Scheduled for Public Hearing by the Board of Supervisors on December 6, 2011

Dear Mr. ~~Griffin~~: *Tony*,

In letters dated September 27, 2011, and October 18, 2011, the City of Falls Church shared with you and the Board of Supervisors its very serious concerns with the County's proposed regulation of the water rates of the City and other localities whose systems serve Fairfax County residents and the proposed exclusive service area for Fairfax Water, which would often require developers to bear the extraordinary cost to construct duplicative water mains alongside the City's existing ones in order to connect to Fairfax Water. To date, we have not received a response to these concerns. On behalf of the City Council I write to outline the likely consequences of enactment of this Amendment, and to request that the County Board defer action on December 6, 2011 to allow a reasonable time for a response to these concerns and to explore more constructive alternatives.

A Mutually Beneficial Relationship

For 80 years, the City has provided safe and reliable water service to citizens of Fairfax County. City leaders issued debt and took on financial and operational risk in order that Seven Corners, McLean, Merrifield, and Tyson's Corner, the economic engine of the County, could develop. Fairfax County has reaped billions of dollars in tax revenue from the resulting commercial development.

The City has been responsive to its customers in the key areas of reliability and rates. For example, the City invested \$20 million in upgrades in the Tysons, Merrifield, and Dunn Loring areas in the past five years in order to improve storage capacity and pressure. We are working closely with developers on redevelopment plans, and we are ready to serve the tremendous new residential and commercial growth that is expected in the Tysons area with the Silver Line, which will provide substantial tax revenue to Fairfax County.

City water rates are lower than average for water utilities in the region, and in the lowest quartile statewide. We were able to make tremendous upgrades to pumping and storage capacity, SCADA upgrades, and security upgrades while keeping rates flat for six years. The

8% increase in water rates enacted this fall by the City Council compares very favorably with the 33% increase in rates that Fairfax Water has implemented over the period since the City last raised its rates, and the 80% increase in sewer rates the County has enacted over the same period.

The City has for decades charged the same water rate for County and City water customers. Under standard utility rate making principles, many municipal utilities charge a higher rate to customers located outside their corporate boundaries. The Supreme Court strongly affirmed this practice last year in *Town of Leesburg v. Giordano*, where a 100% rate differential was in question. The City has charged uniform rates since 1974.

To date, the City has received no formal communication from County staff to explain the purpose of the proposed Amendment, or respond to the concerns raised in the City's earlier correspondence. What follows are the likely results if the proposed Amendment is enacted.

Cost of Water Service Will Go Up

The proposed Amendment is based on the assumption that it will cause water rates charged by the City and other municipal water providers to County residents to go down. This assumption is incorrect. Rates are driven by costs, and this proposed Amendment will increase costs for the following reasons:

First, the proposed Amendment would impose duplicative and redundant administrative costs on municipal water systems: (i) each of the municipal water providers in the County already spends significant sums on professional rate studies prior to an adjustment in its rates, (ii) the proposed Amendment would require each municipality to expend money a second time to go through the County rate process, and (iii) customers in Fairfax County would not have a right to challenge rates under the proposed Amendment, so it is possible that the regulated municipalities could be faced with a third judicial rate proceeding from customers in Fairfax County over the same proposed rates. These additional legal and administrative costs incurred by the municipal water systems would be borne by the citizens of Fairfax County in the form of higher rates.

Second, the mandate to hook up to Fairfax Water will require the construction of a duplicative water system that overlaps with the City's system. The costs of building that duplicative system will be passed on to County water customers of Fairfax Water in the form of higher rates. If the costs of constructing the redundant water system are borne by developers, those costs will be borne by their future tenants and owners.

Third, the cost of capital will increase due to uncertainty involved in having water rates set by what the rating agencies will likely view, any protests to the contrary notwithstanding, as a biased and political regulatory agency. A credit downgrade will increase the cost of capital for the water system, or cause the City and other municipalities to avoid the capital markets altogether, either of which will increase costs for County customers.

Fourth, if the proposed regulation of City water rates by the County renders the continued operation of the system infeasible, the City will likely have serious discussions with its citizens and other stakeholders about a sale of the City's water system to an investor-owned utility, or the creation of a water authority and sale of the system to such an authority. Fairfax County clearly has no ability to regulate the rates of either a privately-owned utility (regulated by the State Corporation Commission) or a Falls Church Water Authority. The State Corporation Commission allows privately-owned water systems to earn a return on investment and charge appropriate rates to their customers.

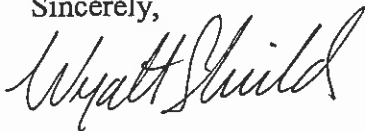
Fifth, as we stated in previous correspondence, the City may challenge in court the assertion of County authority over legislative actions by the City Council. The City may also challenge the mandatory hook up to Fairfax Water, which would impose an extraordinary financial burden on the business community, and leave our existing customers with the stranded costs of prior capital investments in pumping capacity and storage to serve growth. The proposed Amendment will likely trigger litigation expenses that will be borne principally by County residents and taxpayers.

In summary, the proposed Amendment will cause a number of negative results, the net result of which are that the provision of water service in the County will be more expensive for County customers, not less.

Continuing A Mutually Beneficial Relationship

The City asks that the Board of Supervisors defer action on the ordinance to allow time to engage with the City and the other municipalities in the County in a constructive manner. Adoption of the proposed Amendment on December 6, 2011 would be understood by the City to mean that the County does not wish to engage constructively with its partners on water issues, and the City will chart its course accordingly. I think we both believe that there are alternatives that would be worth exploring together that would be mutually beneficial, ensure safe and reliable water for County residents, and reflect the value of the City water system.

Sincerely,

A handwritten signature in black ink, appearing to read "Wyatt Shields". The signature is fluid and cursive, with the first name "Wyatt" being more prominent than the last name "Shields".

Wyatt Shields
City Manager

cc: Council Members, Falls Church City Council
Board Members, Fairfax County Board of Supervisors
Charles Murray, General Manager, Fairfax Water
Board Members, Fairfax Water